A.I.D. Technical Report No. 6

Export Promotion in Indonesia

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FOREWORD

Recent economic literature strongly suggests that outward-oriented economies with sound trade, investment, and export systems have achieved better development results than have inward-oriented economies. The Agency for International Development (A.I.D.) has devoted substantial resources to supporting outward-oriented growth through projects focused on export and investment promotion. Two key questions face donors: Is export and investment promotion assistance worthwhile? Does it merit continued A.I.D. support?

The Center for Development Information and Evaluation (CDIE) has conducted a worldwide assessment of A.I.D.'s experience with export and investment promotion services to evaluate the contribution of intermediaries providing services to exporters in developing countries. Such services include those provided directly to exporters or investors: information (e.g., foreign markets), contact making (e.g., with buyers), deal making, technical assistance, and government facilitation. Issues analyzed include the rationale for donor intervention; the impact on exports, jobs, and the market for support services; the return on A.I.D.'s investment; service strategies; and effective service providers. This analysis has been based on surveys of exporters in seven countries, extensive interviews with service providers, and other sources.

The CDIE assessment focused initially on export and investment promotion projects in the Latin America and the Caribbean (LAC) region. A desk review examining 15 projects resulted in a report, Promoting Trade and Investment In Constrained Environments: A.I.D. Experience in Latin America and the Caribbean, A.I.D. Evaluation Special Study No. 69. CDIE followed up with field visits in Guatemala, the Dominican Republic, Costa Rica, and Chile, culminating in a synthesis report, Export and Investment Promotion: Sustainability and Effective Service Delivery. A.I.D., Program and Operations Assessment Report No. 2. In 1991, CDIE initiated fieldwork in Asia, examining programs in India, Indonesia, Korea, and Thailand. This report is one of four country studies produced for the Asia phase of the assessment. To complement these country studies, CDIE completed two cross-cutting technical reports, "Service Use and Impact: Evidence From Survey of Exporters in Asia," and "Measuring the Costs and Benefits of Export Promotion Projects." In addition, CDIE undertook a desk review of similar projects in the Near East region resulting in the report, "A Review of A.I.D. Experience: Export and Investment Promotion in Egypt and Morocco." The forthcoming program assessment report, "Export and Investment Promotion Services: Do They Make a Difference?" will draw on each of these technical reports in presenting key findings, conclusions, and management implications of this assessment.

SUMMARY

The experience of Indonesia demonstrates the importance of policy and regulatory reform to export growth. A combination of macroeconomic and sector-specific reforms, implemented gradually, was effective in attracting foreign capital and in introducing competition in hitherto closed or constrained sectors of the economy. Trade and investment liberalization was a major catalyst for the accelerated acquisition of foreign technology, finance, management skills, and market contacts required to become competitive in overseas markets. The growth of Indonesian exports was accompanied by the increasing internationalization of the local business community and the rise of a market for the provision of nonsubsidized export promotion services and information.

This study assesses the range of export promotion services in Indonesia from the perspectives of service providers and the firms using such services. Factors considered include the source of services, their use and impact, and the nature of competition in the market for services and information. The study also examines the Agency for International Development's (A.I.D.) limited experience in assisting export promotion in Indonesia during the 1980s. The Agency's support for export promotion came through its bilateral Private Sector Development project, which was far less successful in directly assisting Indonesian firms to export than in contributing to research and development on policy reform and in providing opportunities to the private sector for management training. The findings of the study include the following:

> Policy reform was an important precursor to the development of an indigenous export capability. USAID/Indonesia's assistance in deregulation throughout the 1980s played a more substantial role in effecting change than did its direct interventions to support firm-level activity.
>
> Government-subsidized export promotion programs were of some help to exporters at the early stages of firm market entry (e.g., buyer contacts, trade fairs, general market information), but were marginal at later stages, when more technical and market sensitive expertise is needed. Government-managed investment promotion had no impact.
>
> The majority of export firms rely heavily on internal resources and highly interrelated seller/buyer relationships, and little on the fee-for-service market for export assistance. Kin, associates, and dominant buyers provide production, market, and financial assistance to entrepreneurs, who still largely eschew fee-based advisory services.

GLOSSARY

A.I.D. - Agency for International Development

BKPM - Indonesian Investment Coordinating Board

BRD - Buyers Reception Desk, a program of the Ministry of Trade

CDIE - Center for Development Information and Evaluation

ESB - Export Support Board, a program of the Ministry of Trade

GDP - gross domestic product

IEDF - Indonesian Executive Development Fund

IETC - Indonesia Export Training Center

JETRO - Japan External Trade Organization

JICA - Japan International Cooperation Agency

LAC - Bureau for Latin America and the Caribbean

NAFED - National Agency for Export Development, a Ministry of Trade agency

NIC - newly industrialized countries (Hong Kong, Singapore, South Korea, and Taiwan)

OECD - Organization for Economic Cooperation and Development

PSD - The A.I.D. Private Sector Development project

UNIDO - United Nations Industrial Development Organization

UNDP - United Nations Development Programme

USAID/Indonesia - A.I.D. Field Mission

1. STATEMENT OF THE PROBLEM

During the past several decades, developing countries that maintained an outward orientation have achieved economic growth much faster than countries that relied heavily on import substitution. In the 1960s, A.I.D. was a leader in promoting export-led growth in developing countries. Again in the 1980s, under the Private Sector Initiative, A.I.D. gave strong emphasis to trade liberalization and outward-oriented growth. The Agency devoted substantial resources to policy reform and to projects providing export and investment promotion services. Most development experts agree that appropriate economic policy is crucial to outward-oriented growth, but there is still considerable debate about the contribution that export and investment promotion services can make to reinforce policy. The following questions demand further analysis:

Is a favorable policy environment enough, or can promotion services to exporters and investors accelerate export growth?

If promotion makes a useful contribution, which services and what kind of providers are most effective, and what is the justification for donor support?

This study of Indonesia is part of a larger assessment to examine A.I.D. experience with export and investment promotion services worldwide. The first phase of the assessment examined projects in Latin America, focusing on successful programs in favorable policy environments. The current phase examined promotion services in four Asian countriesþIndia, Indonesia, Korea, and Thailandþwhere A.I.D. carried out projects in differing policy environments. The assessment included a survey of nearly 300 exporting firms, including 48 in Indonesia. The aim was to identify the services exporters actually used, which ones made a significant difference to export success, and who provided the services.

This report examines the role of export promotion services in supporting the transition from an inward to an outward orientation. It tries to determine whether there are gaps in this market and, more specifically, whether there is a case for the intervention of donors to subsidize, directly or indirectly, such services. Special attention is given to an assessment of A.I.D.'s $10 million bilateral Private Sector Development (PSD) project, which, over a period of 7 years, struggled with various approaches to direct assistance for export and investment promotion. The central question in the Indonesian case is whether firm-level assistance is an important adjunct to reform of the policy regime.

2. THE ECONOMIC CONTEXT

2.1 The Policy Environment and Deregulation

Since 1966, when a coup d'etat ended years of economic disorder and confused policies, Indonesia has maintained a stable economic policy environment. Indonesia's economic performance has been enormously impressive, with per capita income more than tripling. Massive oil revenues during the 1970s made much of this growth possible. The decline and collapse of oil prices after 1980, however, destabilized the economy and called into question the dependence on oil exports for financing government spending and capital-intensive investment. Between 1980 and 1988, the share of the oil/natural gas sector plummeted from 26 percent to 19 percent of gross domestic product (GDP). It plummeted from contributing more than 75 percent of foreign exchange earnings to 39 percent, and from providing nearly 70 percent of central government revenue to 41 percent.

This crisis led Indonesia in the 1980s to undertake a series of economic reforms, whose overall impact was sweeping. Financial sector reforms sought greater competition within the sector and stronger linkages to the international financial system. A comprehensive tax reform reduced reliance on oil taxes, external finance, and foreign aid. Seeking to increase incentives for the private sector, Indonesia revamped the regulatory structure for trade and investment. The reforms eliminated or liberalized restrictions on foreign investment and simplified and made more transparent procedures for doing business in Indonesia. Although the new regulations declared equality of treatment of foreign investors with Indonesian investors, they assured local entrepreneurs of benefiting from deregulation and profits from technology transfer, management training, and international market contacts. Thus, liberalization was tempered by a strong current of nationalist sentiment that persists.

International trade was liberalized. Quantitative controls, registration and licensing requirements, sector exclusions, tariffs, nontariff barriers, and complex customs procedures were all examined and reformed after 1985. Tariffs were lowered, licensing was broadly liberalized, and the quota system was reorganized to introduce some flexibility. The reforms, a top-down process, were administered incrementally and received with little popular backlash, considering that the loss of protection and the introduction of new competition meant that the distribution of wealth would change. "Deregulation and Export Incentives," available separately from the A.I.D. Library as Section C of CDIE Working Paper No. 151, provides more detail on the relationship between deregulation and export encouragement.

The Indonesian exchange-rate regime was also gradually reformed. Under the pre-1966 regime, potential foreign investors and exporters faced a bewildering system of multiple exchange rates, exchange controls tied to a complete licensing system, and a greatly overvalued rupiah. In 1966, the rupiah was devalued and exchange controls loosened. Exchange controls were eliminated entirely in 1970. Inward and outward private flows are now free and unrecorded. The rupiah fluctuates based on a basket of currencies.

2.2 Export Performance

Indonesian export earnings have historically depended on oil. As shown by Figure 1, total export earnings declined during the 1950s and 1960s, but rose sharply following the 1973 oil price increases. Export earnings peaked with oil prices in 1980, and exports fell dramatically during the first half of the 1980s. Some recovery took place during the last half of the decade, but 1990 export earnings were still lower in real terms than at the beginning of the decade.

Nevertheless, a great deal happened during the 1980s to end Indonesia's dependence on oil. Figure 2 shows the commodity composition of exports to the industrial countries. The predominance of oil is clear, as is the relative insignificance of manufactured exports until the mid-1980s. By 1990, oil and natural gas exports were down to half of total exports to industrial countries. The dramatic growth of manufactures following the overhaul of macroeconomic and trade policy is shown in Figure 3. Manufactured exports to the industrial countries tripled to $5.9 billion between 1985 and 1990, and manufactures were beginning to challenge oil as a source of export earnings.

This rapid growth in manufactured exports is rapidly changing Indonesia's industrial structure. Between 1985 and 1990, shoe exports to the Organization for Economic Cooperation and Development (OECD) countries grew from $4 million to $563 million, furniture exports from $8 million to $290 million, and textiles and clothing exports from $400 million to $2 billion. Steel, plywood, paper, glass, rubber products, and a host of other categories of exports also grew dramatically. Plywood and wood product exports have benefited from a 1985 ban on log exports, but the breadth of the strong export performance shows rapid growth in manufacturing competence on a wide front.

The United States, which takes 30 percent of manufactured exports, has been Indonesia's largest single market, but the export growth shows considerable geographical diversity. Much of the export thrust of the 1980s has been stimulated by inflows of foreign investment. Japan has been the largest source of foreign investment in Indonesia, with $6.5 billion in investment approvals from 1967 to 1989, but since 1986 investments from the newly industrialized countries (NICs) of AsiaþTaiwan, Korea, Hong Kong, and Singaporeþhave been increasing rapidly. These investments and export growth appear to be due to the cascading of production within Asia, as lower skill jobs move from the NICs to lower wage countries. Indonesia is well placed for this, offering low-average wage rates, a freely convertible currency, a successfully deregulated and now comparatively liberal business environment, and important natural resources.

2.3 The Private Sector and Constraints to Exports

During the early 1980s, the Indonesian export sector faced a number of constraints that prevented it from fully exploiting export opportunities. For example, numerous areas suffered from weak macroeconomic policy, firms had inadequate knowledge of the technical aspects of production and of international markets, and potential foreign investors lacked information on opportunities in Indonesia. Nevertheless, the rapid growth of Indonesian exports since 1985 shows that these constraints have not been as severe as to prevent export growth.

3. THE MARKET FOR EXPORT PROMOTION SERVICES

3.1 Background

The rapid growth of nonoil Indonesian exports demonstrates that Indonesian firms rapidly increased their competence and capacity to produce and market products in the intensely competitive international marketplace. Did firms acquire these skills more or less automatically with improvements in economic policy and more favorable exchange rates, or were other factors important? How, and from whom, did they acquire the necessary skills and services? The survey portion of this study covers the following four sets of issues of direct relevance to providers of export-related services and to donors considering financial support:

Overall Service Use. What types of services do firms use, how does use correspond to business needs, and how does use change with stages of market entry?

Source of Services. Where do firms obtain the services they consider important?

Impact of Services. What impact do services have on a firm's performance?

Service Mix. What mix of promotion services is most effective in supporting export and investment success?

For this study, interviews were carried out with a number of small- and medium-size Indonesian exporting companies ($100,000 to $10 million in annual export sales), and with a number of organizations providing services to exporters. Forty-eight firms, 38 in light manufacturing, served as the firm-level sample for this study. Most of the firms were located near Djakarta. At best, the selected firms constitute a representative sample, weighted to reflect the 1990 distribution of nonoil exports and drawn to include some A.I.D. -assisted firms. Most of the firms began exporting after 1985; therefore, they have recent experience with the search for contacts, skills, information, and markets. The major focus of this study is with services used by local firms for export development. The study examined A.I.D.'s experience in assisting export and investment activities since the mid-1980s.

3.2 A.I.D.'s Approach to Assisting Export Promotion

During the early 1980s, USAID/Indonesia discussed with the Government possible assistance for policy reform and for other measures to involve the private sector in Indonesia's development process. These discussions resulted in a 1982 project comprising a cluster of exploratory activities aimed to eventually position A.I.D. as a key donor in assisting the private sector. Based on only limited analysis of private sector issues, the PSD project assumed that the Government of Indonesia was politically committed to improving the business environment through deregulation, that this environment also operated against numerous nonpolicy constraints, that Western technology and U.S. management education were needed, and that U.S. investment in Indonesia could be increased by A.I.D. financial support.

Providing U.S. professional expertise and brokering Indonesian/American business contacts and transactions were key objectives of this 7-year activity. The project was funded at $9.6

million, of which $7 million was allocated for three activities reviewed by the evaluation team. These activities are briefly described below; their effectiveness is assessed in Section 4.

1. Facilitating Foreign Private Investment. In the early 1980s, the Indonesian Investment Coordinating Board (BKPM) was charged with planning, prioritizing, and promoting investment programs, including reviewing applications and issuing licenses. Most important, the BKPM issued the annual Investment Priority List, which specified which business areas were open or closed to foreign investment and which were to receive high or low government priority. The PSD project was intended to fill a gap between BKPM, which sought to market investment opportunities and foreign, particularly U.S., investors. Selected Indonesian consulting firms having a U.S. partner were expected to play a brokering role.

To implement the project, the BKPM contracted with three consulting firms having U.S. business connections. The firms were to compete with one another in facilitating joint-venture investment transactions, primarily between U.S. and Indonesian partners. The consulting firms would provide project identification, partner search, proposal preparation, technical assistance on regulatory issues, and government facilitation. Up to 25 free consultant hours were to be provided to selected businesses, favoring projects with an export component. A.I.D. expected that the project would allow the three consulting companies to develop long-term relationships with U.S. clients for repeat business.

The BKPM's Investment Priority List was to guide investment to those priority sectors favored by the Government, and the project was to finance up to 30 project profiles in the priority sectors. These profiles were expected to serve as feasibility studies that could attract needed U.S. investments. Other donorsþUnited Nations Industrial Development Organization (UNIDO), the World Bank, and the Canadian International Development Agencyþhad also been financing project-investment profiles. A.I.D. provided $2 million for this component of the project.

2. Management Training. A.I.D. believed that Indonesia's business community lacked the necessary management skills to take advantage of new opportunities. Few Indonesian entrepreneurs or firm managers were exposed to modern management education or had the opportunity to visit the United States. The PSD project funded training for the private sector and created business ties between the United States and Indonesia. The project included a $500,000 grant for the Ministry of Finance to fund short-term, mid-career, and advanced training at U.S. business schools. This training program, called the Indonesian Executive Development Fund (IEDF), included training courses, seminars, workshops, tours of businesses, and hands-on management internships. The Government of Indonesia contributed $1.3 million to a low-interest loan fund to help participants meet the costs of their travel and stay in the United States. The loans, meeting up to 75 percent of costs, were to be repaid within 5 years of the participant's return. Initiated in 1985, almost 60 firms applied in the first year and about 35 participants actually traveled.

3. Special Studies and Consulting Services. The PSD project included $4.5 million for analyses and technical consultancies aimed at improving the business climate. This included strengthening institutions responsible for policies and services affecting private -sector activities. Target activities were tax reform, capital market development, central banking, and investment instruments such as venture capital.

3.3 Use and Impact of Export Promotion Services

This section provides the main results of the survey of 48 Indonesian exporting firms with respect to their experience with export services. Considerable additional detail, as well as methodological description of survey procedures, is included in "Service Use and Impact in Indonesia," available separately from the A.I.D. Library as Section A of CDIE Working Paper No. 151.

Both local and foreign firms found a variety of services important to their success. They used both intensive, customized services like technical assistance for production and sample preparation, as well as more standardized services like country and market information. The average firm used 12 services. Firms considered about three-quarters of these services to have had an impact on the firm's success. Foreign firms used services slightly more intensively than did local firms. There was considerable variability among firms in service use, however; therefore, it is difficult to determine a priori which services a particular firm would find most valuable. Table 1 lists all the services that the firms considered to have had an impact on their success. Local firms and foreign investors gave similar importance to some services, but differed on others. Buyer contacts, market

Table 1. Percentage of Surveyed Firms Valuing Services Highly

	Firms	
Impact Rank	Local	Foreign
1. Production Assistance	85	80
2. Buyer Contacts	82	53
3. Marketing Assistance	64	60
4. Information/Country	61	60
5. Sample Preparation	64	47
6. Market Information	64	40
7. Training	45	73
8. Information/Sector	45	53
9. Trade Shows	55	13
10. Directories	42	33
11. Management Assistance	36	40
12. Overseas Representation	30	33
13. Approvals/Paperwork	21	53

14. In-country Questions and Answers	36	20
15. Credit Facilitation	30	27
16. Firm-specific Research	21	47
17. Accounting Assistance	21	40
18. Legal Assistance	9	53
19. Deal-making Assistance	6	40
20. Customs Assistance	3	47
21. Site Visit Support	3	40
22. Government Contacts	6	27
23. Proposal Development	9	20
24. Lobbying/Policy Change	6	0
25. Feasibility Studies	3	7
26. Trade Missions	3	0
27. Financing for R&D	3	0
28. Other Preexport	0	7

Source: Study Survey

information, and trade shows were of more value to local firms, whereas training assistance was more important to foreign firms. Feasibility studies, trade missions, and lobbying/policy change were important to neither.

The survey data also suggest that no single service provider can meet all the needs of a local exporter or foreign investor. Local firms rely on their internal resources as well as on private-sector and government sources. Local government agencies play a key role in trade shows. Personal contacts, however, often put foreign and local firms in contact with joint-venture partners. Depending on the sector and timing, firms used a variety of service providers to make their exports or investments happen.

Table 2 shows where firms acquired the services with significant impact. Buyers, suppliers, and partners (both local and foreign) as well as internal resources were viewed as most critical by both exporters and foreign investors. Government agencies provided some valuable services for exporters but none for foreign investors.

Intensive, customized, and high value-added services (technical assistance for production and marketing, sample preparation) are handled mostly by internal sources or buyers/partners. More than half (58 percent) come from internal sources and about 30 percent from buyers.

Internal firm resources and buyers/partners also provide more than two-thirds of standardized services (market information, buyer contacts, information about a country). However, government agencies and chambers of commerce play a more important role and provide nearly 30 percent of these services as well.

In addition to the specific questions on sources of services, each interviewed firm was asked to distribute the credit for its export success among the institutions involved. Firms attributed 55 percent of their success to their own efforts, and allocated the other 45 percent among other organizations. Table 3 summarizes the distribution of credit given to external organizations. The results broadly track those of Table 2. Most credit is given to business partners, followed by private-sector sources. In the latter category, Indonesian firms gave credit mainly to not-for-pay services (e.g., industry associations and chambers of commerce), whereas foreign firms mainly used paid services, such as consulting firms. Indonesian Government programs received considerable credit from local firms, but not from foreign investors. Foreign government or international donor programs were of marginal importance, given credit mainly by foreign investors.

Other findings from the interviews include the following:

1. Local firms seem to benefit most from services at the early stages of exporting. Buyer contacts are particularly important. Once buyer relationships are developed, buyers provide services farther down the export process (e.g., sample preparation and production, technical assistance).

Table 2. Sources of Highly Valued Services

Export Services	(%)	Foreign Investment Services	(%)
Internal Sources	34	Buyers/Partners	44
Buyers/Partners	32	Internal Sources	36
Government Agencies	16	Private Sector/No Fee	12
Private Sector/No Fee	13	Private Sector/Fee	8
Private Sector/Fee	5	Government Agencies	0
Total	100		100

Source: Study Survey

Table 3. Attribution for Success in Exporting
(percentage)

	Firms		
Source	Local	Foreign	Total Sample
Buyers/Suppliers/Partners	51	63	55
Private Sector	21	16	20
Indonesian Government	24	10	19
Foreign Governments/Donors	4	11	6
Total	100	100	100

Note: Attribution calculations exclude attribution to sources internal to firm (45 percent of total success for local firms and 41 percent for foreign firms).

Source: Study Survey

2. Services that have the highest impact on foreign firms are those provided at the beginning (e.g., country identification) and later in the investment promotion process (i.e., pre-investment preparation and start-up). In joint ventures, both partners play a key role in providing these services. Notably, foreign investors gave the Indonesian Government no credit for providing useful investment service (see Table 2). Local partners provide country and sector information as well as assistance in government approvals. Foreign partners provide technical assistance and training services.

The actual linking of local and foreign firms ("deal making") was not cited among the 10 most important services. Where it was mentioned, 67 percent of firms interviewed used unpaid private -sector sources, such as chambers of commerce; 22 percent paid for services of a consulting firm; and 11 percent used government agencies.

3. A.I.D.-financed services did not have much impact on the "assisted" group of firms. Overall, only about 3 percent of the highly valued services received by "assisted" firms were provided by A.I.D. -financed firms. There was no significant difference between the projected export-growth rates of unassisted and assisted firms. Both are expected to increase exports from 1991 to 1995 by about 60 percent.

4. The private sector (principally buyers and suppliers) is very active in providing important services. Overall, local firms received more than 50 percent of their services from private-sector sources and only 12 percent from the public sector. Foreign firms received more than 60 percent from private sources and only 5 percent from public-sector sources.

5. Local firms have a strong desire to shift their export -market base toward the U.S. market and away from their current (80 percent) dependence on Europe and Japan. By 1996, local firms want to double their U.S. market share to about one-third of total exports. Agroprocessing firms also want to diversify into higher value-added products that use more sophisticated technology. Both were considered to be best provided through a joint venture with a foreignþparticularly a U.S.þfirm.

6. The survey suggests significant positive externalities and spillover effects resulting from assisting local firms to export. Among the more significant findings are the following:

More than 40 percent found the information gained from studying other export firms to have been "very useful" or "critical."

More than 60 percent believe that their firm's entry into the export market benefited other competing firms.

Close to half the local firms claim that their export experience resulted in improvements in the management and quality of products destined for domestic markets.

> More than 50 percent of local firms that started up in exporting had some previous export experience either through other manufactured exports or trading companies.
>
> About 75 percent of the respondents claim that their initial success in exporting led more than five other firms in the same business to follow their example.

Service use proved to be a complex question. Many factors determine which services are used and how important they are to success. Prior entrepreneurial experience, type of ownership, financial size, ethnicity employed in using networks of associates, and the stage of export market entry all make a difference in the decision -making process. For local firms, however, it appears uniformly valid that the up-front need for buyer contacts and for operational information on penetrating certain markets are critical. Once contacts are firmly in place and an information base established, local exporting firms tend to rely more directly on buyers for production and market-related needs. For foreign firms considering investment, the most highly valued services follow the decision to invest: government approvals, legal assistance, and official contacts.

The four main findings from the survey include the following:

> Buyers make exports happen. Buyers are to local exporters as location is to a real estate broker. Buyers are critical to a local firm's export success. Through buyers, local firms can acquire market information. Buyers also assist with sample preparation and technical assistance for production. Contact with buyers can provide local exporters with many of the most important services required to export.
>
> Partners are critical to both the export and investment process. This is particularly true for foreign firms trying to invest in Indonesia. Legally, foreign firms need to have local joint-venture partners. Practically, both the foreign and local joint-venture partners rely on one another for important services. Foreigners provide production and marketing technical assistance. Local partners provide government contacts and information on regulations, paperwork, and local conditions.
>
> The private sector was key to finding Indonesian partners for foreign investors, but both the private sector and government agencies helped Indonesian firms find buyers. Information on local partners for foreign firms was spread among several sources including personal contacts, private consulting firms, chambers of commerce, and overseas embassies. The National Agency for Export Development (NAFED) was a key source for buyer contacts.
>
> The scope of government programs should be limited. The survey shows that government agencies can be most helpful in providing general information services (e.g., country and sector specific) and in providing buyer

contacts. Government should not be expected to get involved in providing firm-specific services: technical assistance, sample preparation, and market information. These are best left to buyers and partners.

3.4 Service Delivery: The Role of Service Providers

Surveyed exporting firms identified internal resources and buyers as the two main sources of export promotion services. In fact, the overall market for export promotion services shows considerable diversity, which, in some segments of this market, is quite recent in origin. Not surprisingly, the growth of activity in this service market parallels the increase in Indonesian export activity. In the early 1980s, during the inception of the PSD project, the business climate in Indonesia was not conducive to private sector export initiatives. However, as discussed elsewhere, the 1980s opened investment and trade opportunities, creating niches for entrepreneurial starts in the area of nontraditional exports.

The assessment team interviewed more than 30 service or information providers, giving most attention to consultant firms and producer associations. In retrospect, more importance should have been given to bilateral chambers of commerce, trading companies, agents of foreign buyers, and Asian joint ventures, since they appeared to be effective service and information providers. Although not part of the interview group, Indonesian Government agencies were also studied.

This part of the study was initially guided by the following three concerns:

Did there appear to be market failures in the provision of key services or information?

Was there a justification for bilateral donors to directly or indirectly promote exports of nontraditional manufactures? A.I.D.'s past intervention and present initiatives were examined, and programs of Japan, Germany, and the Netherlands were examined in some detail.

Does export service provision create positive externalities (e.g., bandwagon effects) for the export sector? Because of inadequate data, the results are only suggestive of a positive finding in this area.

No secondary-source material exists on the evolution of the market of service and information providers over the past decade, a decade that has witnessed extensive progress in establishing a favorable environment for Indonesian exports. Characteristically, the few better established consulting firms, early on, emphasized engineering services, concentrated on oil and gas exports, generally relied on expatriate expertise, and had no strategic interest in helping indigenous firms access foreign markets. Until recently, there were few specialized firms offering export-related professional services, such as accounting, legal, insurance, or financial products, in addition to their domestic work.

The rise in the number of consulting firms during the past 5 years has partly grown out of increased government and donor -financed projects, which generated the need for feasibility or technical studies related to development projects. These firms have tended to diversify from engineering to broader business advisory services and then toward facilitation of direct foreign investment. Despite expatriate influence in many of the firms, current government restrictions appear to limit the potential for major increases in foreign entry into this services market. The consultant rate structure is below international standards and the percent of consultant time offered by expatriates as a percentage of the firm's total time is also set by the Government. Work permit restrictions can be evaded, but add to the general list of constraints facing the internationalization of the services market.

Most of the firms surveyed are multiproduct in nature and are often in competition with one another and with the few government agencies that overlap with private-sector entities. Even government organizations at times duplicate one another either in targeting the same sectors or in the type of services provided. Profits, in this setting, are enhanced by locking a client into buying a sequence of services, which begins with market surveys and continues through to structuring the financial package. For the foreigner, paying for consultant services is an acceptable practice. For the local entrepreneur, free advice or assistance tied to the commission of a successful transaction is more the norm. Fee rates are currently stable, if not declining, in real terms.

Despite the multiproduct character of firms, there is important differentiation in this market. The following highlights are taken from Section B (taken from CDIE Working Paper No. 151) and from interview results.

Consulting Firms. Many larger, established consultant firms with an expatriate element still concentrate on securing government and donor contracts. Only a few have made significant profits in brokering the occasional, large investment transaction for foreign firms. A smaller number still are involved in handling the export needs of indigenous businesses. Small Indonesian export firms continue to be reluctant to pay for consultant services, nor do they represent a lucrative clientele for big firms with high overhead. There is a growing number of small Indonesian consulting firms, often heavily staffed by new business-school graduates. These firms generally rely on government and donor contracts. To date, foreign investors are more comfortable dealing with firms with expatriate experts.

Producer Associations. Producer/manufacturing associations exist in most sectors. They range from the moribund associations that have long existed only on paper in response to government regulations to really active entities, such as those for rubber processors and leather-goods manufacturers. Yet others, such as the plywood manufacturers determined to maintain their protected status, are organized around cartel operations. At their best, they provide members with information on production technology and market conditions. Foreign buyers appear to avoid these associations, considering them weak and constrained by bureaucracy. In certain industries, such as fisheries, international health and packaging standards are critical issues. Here, problems are effectively approached through the association rather than through individuals. In general, associations appear to lack the technical capacity to be key resources for their membership.

Government Agencies. Government agencies in Indonesia have historically failed to provide effective export promotion services. As described below, the success of the A.I.D. PSD project was adversely affected by the role of the BKPM as a regulator of foreign investment. The BKPM was never staffed or organized to deal effectively with the private sector in an investment or export promotion role. The recent efforts of the Ministry of Trade seem more promising. The Ministry is actively seeking an active role in export promotion. Its NAFED has targeted small and medium businesses as beneficiaries of its services. NAFED is finding a niche in arranging trade missions and trade fairs for relatively new-to-export companies. It also facilitates foreign-buyer contact with appropriate local producers. The Ministry of Trade is actively trying to upgrade its professional staff and to pare back to a concentration on assistence to firms newly entering into export production.

Bilateral Chambers of Commerce. Several countriesþnotably Japan, the Netherlands, and Germanyþhave developed close interaction between embassyþcommercial operations, an in-country membership chamber of commerce, their own export/import agencies, trade-related financial institutions, and aid agencies. In each case, in addition to facilitating exports to Indonesia through buyer/investor contacts, they have activities to strengthen Indonesian capacity to export to or through their country. They expend considerable effort to provide technical information on design and standards as well as the regulatory situation prevailing in their country. For example, they sponsor trade missions and fairs with a capacity to follow-up on contacts leading to a transaction. For all three countries, there is an overt, comfortable relationship between foreign policy objectives and private-sector interests.

Foreign-Buyer Services. The many joint ventures that particularly characterize Asian investments in Indonesia are perhaps the most effective vehicles for export assistance. These close-knit relationships often contain the full range of services needed to develop a potential export. Most Japanese partnerships of this type are initially assisted by the network of public and private Japanese interests described above. They converge to place Japanese technicians and managers within Indonesian firms and to ensure quality and timely delivery of goods to the Japanese marketplace. Beyond these carefully brokered firm-to-firm relationships, the Japanese are sponsoring trade missions and fairs for Indonesian goods and training programs stressing quality control and Japanese management techniques. The number of such broad spectrum arrangements is unknown, but clearly they account for a major part of Indonesia's trade with Japan in manufactured goods. This is discussed in more detail in Section C of CDIE Working Paper No. 151, "Deregulation and Export Incentives."

Other. The case of the foreign buyer working through a resident agent is akin to the joint-venture case discussed above. The agent is often responsible for a broad range of services, such as identifying promising suppliers, sharing design or packaging information with the exporters, and ensuring that product quality and delivery meet buyer expectations. According to A.I.D.-sponsored research, trading firmsþthe once important Indonesian export/import housesþaccount for only 12 percent of Indonesian nontraditional exports. Section B of CDIE Working Paper No. 151 summarizes the interviews with service providers. A few government firms specialize in quota-based trade (spices and coffee). Overall, trading firms have not been an innovative modern force in stimulating exports.

As indicated, there is considerable overlap among providers of export promotion services. Service availability has expanded and is likely to continue expanding. For sectors in which there is market potential but exports are not significant, firm-to-firm "hands on" assistance has been an efficient means of boosting exports. Intervention in this market has followed the avenue of mutual profit seeking between buyers and sellers.

4. EFFECTIVENESS OF EXPORT PROMOTION INTERMEDIARIES

4.1 The A.I.D. Private Sector Development Project

Indonesia's investment and export climate of the early 1980s was the backdrop for A.I.D.'s early efforts to work with the private sector. A prolonged recession, due to falling oil prices, triggered austerity measures and a curbing of public investment. As the rupiah declined against the U.S. dollar, monetary stability became questionable. Tough foreign equity and divestiture requirements, coupled with a widely perceived inequity in the application of deregulation measures, further served as disincentives for the entry of foreign investments. Despite higher costs of production, other Asian countries appeared to be more hospitable business environments to U.S. investors generally unfamiliar with the complexities of doing business in this part of the world and, aside from oil and gas, reluctant to take greater economic and political risks in Indonesia.

The A.I.D. PSD project was intended to be a flexible resource to alleviate a few specific constraints. The project was only one of several approaches employed by USAID/Indonesia and was viewed as a catalyst to initiate other activities related to developing private-sector initiatives. Some exploratory elements were clearly unsuccessful, but others became general contributions to building a more effective enabling environment. The lag between many project inputs and subsequent changes in firm-level performance makes attribution to the project difficult. The measurement of economic returns for the main elements of the project was also not possible because of the lack of supporting project file data and a comparable lack of information in the records of assisted firms. This section reviews the project's performance in key areas:

Facilitating Private Investment. In 1984, after considerable delay, the BKPM let three contracts to consulting firms for preparing project profiles and for providing consultant assistance to both Indonesian entrepreneurs and U.S. investors. Projects identified were to meet Government of Indonesia priorities in agribusiness and light manufacturing. The consultant firms were to (1) prepare project investment profiles; (2) identify promising companies for investment; (3) provide promotional services such as direct mail, leaflets, and business forums; (4) assist in the preparation of investment applications; and (5) undertake partner searches.

The preparation of project profiles was an unsuccessful activity. Other donors had been financing profiles with mixed results. Their efforts, not unlike those of A.I.D., were driven by a general rationale to support investments in areas perceived by the Government of Indonesia as national priorities. Five profiles were done (salt production, pig rearing, glass fiber production, animal feed, and pump manufacturing), but the profiles generated almost no investor interest. In part, lack of interest in the profiles may have reflected low-quality analysis by the consultant firm. More important, however, the BKPM selection of activities to profile was guided by government policy views and not by expectations of economic viability. BKPM also did not aggressively market business opportunities. In 1986, the profiles were dropped from the project on the grounds that profiles, even when done well, could not attract investor interest or commitment let alone respond to the rapidly changing conditions of the marketplace.

The provision of free consulting time to Indonesian entrepreneurs and to U.S. firms also yielded few results. Some 250 inquiries were considered, of which 20 U.S. and 34 Indonesian firms ultimately received free consultant time. Only eight firms received the maximum permitted 25 hours, and only three firms (all U.S. companies) paid for additional hours. Out of all of this activity, only four applications were prepared by 1986 for BKPM consideration. These were battery manufacturing, herbicides, oil drilling equipment, and pump production. Whether any of the four actually resulted in investment is unknown.

Several lessons can be gleaned from these experiences. It should be kept in mind, however, that only the first steps toward effective deregulation and the "debureaucratization" of a highly centralized economy occurred in the early 1980s. Some effects of the PSD project can be noted:

> The Indonesian Government initially conceived of BKPM as an export and investment promotion institution, which proved unsuccessful. BKPM has subsequently developed expertise as a licensing board for investments only.
>
> The performance of consulting firms' contracted under the PSD project was often poor and their efforts ineffective. The inability to deal smoothly with the BKPM, the poor

execution of some of the profiles, the less than adequate contract administration by A.I.D., and the apparent lack of export promotion expertise can be cited for their failure. The primary interest of the consulting firms was not joint ventures in nontraditional exports, but rather the brokering of U.S. investments in the traditional energy sector.

Indonesian businessmen were unaccustomed to paying for consultant time. Advice linked to a commission if the transaction was successful was a more familiar Indonesian form of purchasing promotional services.

Consultancies in some cases helped to initiate a business process. Whether this facilitation was crucial to completing a transaction is difficult to determine.

Management Training. The management training program fared much better. It has evolved into a worldwide program, the Indonesian Executive Development Fund (IEDF), which continues and has sent more than 150 executives to the United States. The visits have included custom-tailored tours of industries and firms, short-term management training, and corporate internships. A.I.D. expected that such training would generate U.S. contacts that would lead to future joint venture and trade links. The evaluation team was unable to find any data that would permit an assessment of this expectation.

In addition to individual training, IEDF facilitated workshops between U.S. counterparts and visiting Indonesian trade delegations. In 1988, Indonesian furniture manufacturers toured the United States to become familiar with import procedures and quality and design issues, and to line up contracts. The A.I.D. contractor, Pragma Corporation, has continued to develop this program on a worldwide basis without A.I.D. funding. Now known as the International Enterprise Development Program, it offers an established program of annual courses, many of which coincide with trade shows.

Special Studies. In many respects the studies and technical assistance component of the PSD project (40 percent of project funds) has had the broadest and longest term impact. A.I.D. influenced the conceptualization and implementation of various Indonesian deregulation packages (further discussed in Section C of CDIE Working Paper No. 151). U.S. commercial interests, as well as the commercial interests of other countries, have directly benefited from a more outward- and liberal-market orientation. The studies assisted key policy institutions important to the private sector. The central bank was assisted on financial reform, capital-market development, and pension fund administration. The Ministry of Finance used the project funds to simplify tax collection procedures and improve administration, benefiting private-sector entities by increasing the uniformity of tax treatment and reducing the discretionary authority of tax officials. In general, the studies appear to have strengthened relationships with key government entities, such as the Ministries of Finance and Trade, permitting A.I.D. to assist and support reformminded policy officials and to provide appropriate technical expertise to strengthen institutions and processes.

In sum, the portions of the A.I.D. project providing training and special studies appear to have had their intended effects, but the investment promotion activity must be regarded largely as a failure. This failure seems to stem partly from the use of a government institution largely concerned with regulating foreign investment as a vehicle for promoting it, partly from the use of consulting firms as promotional intermediaries, and partly from design flaws.

4.2 Other Approaches to Service Provision

4.2.1 The Interested Buyer as Supplier

Asian investments in Indonesia, as noted, are significant not only in volume and value, but in the nature of the buyer-supplier relationship that is formed. The Asian buyer often dominates the joint-venture-type relationship by supplying input components, production techniques, management expertise, needed training, finance, and a monopoly on sales links. These highly dependent relationships obviate the need for external export promotion services. Japan is Indonesia's largest investor with cumulative investment during 1967-1990 of $9.6 billion. This compares to $3.7 billion from Hong Kong, $2.3 billion from Taiwan, and $1.9 billion from South Korea. Japan also serves as an interesting model of buyer dominance and public and private sector cooperation in pursuit of export enhancement. The key players in the Japanese approach are the Economic Section of the Embassy of Japan, the Japan International Cooperation Agency (JICA), the Japan External Trade Organization (JETRO), the Indonesia Export Training Center (IETC), and Japanese importers.

The Economic Section of the Japanese Embassy provides analysis of conditions, facilitates government contacts, refers interested Japanese buyers to programs, and provides in-country support for JICA. JICA is an important element of Japan's bilateral program. About 17 percent of Japan's official aid goes to Indonesia, making it the largest recipient of Japanese aid. In a program closely coordinated with other key Japanese activities, JICA provides (1) experts assigned to the BKPM to facilitate licensing of Japanese investments, (2) two training programs (courses in Japan for groups of Indonesians selected by the Indonesian Government, and tailored training for individual entrepreneurs selected by JICA), and (3) management of the IETC project.

The IETC is a 5-year project started in 1988 to train private -sector manufacturers in such areas as production technology, product marketing (with particular reference to meeting Japanese market import standards), design and packaging, production management, and product testing and quality control. The center specializes in nontraditional exports, such as furniture, textiles, rubber goods, and processed foods. Staffed by 14 Japanese experts and 20 counterparts, this well-endowed institution offered almost 40 courses to nearly 700 participants in 1990-1991. The Center intends to double the number of participants in 1991-1992. This program targets Indonesian companies with a Japanese corporate or market connection. JETRO and Japanese companies not only pay to send selected managers to the program, but often provide their own instructors to ensure results. Meeting Government of Japan and Japanese trade association standards are prime objectives of IETC.

JETRO was established in 1958, with Japanese Government support, as a nonprofit trade organization. Its role in stimulating Japanese exports has been emulated by several Asian countries. The Ministry of International Trade and Industry oversees JETRO's offices in 57 countries and 50 prefectures in Japan. JETRO has now been mandated to promote the flow of imports into Japan, backed by a sizable import promotion budget. In Indonesia, JETRO's activities are fully coordinated with the other activities previously discussed. JETRO carefully places Japanese manufacturing and marketing specialists in selected firms on long-term (2 to 5 year) assignments. The local firm pays about 25 percent of costs of this arrangement, which is intended to develop contracts to supply the Japanese market. In another recent program, JETRO paid for Japanese design experts to spend up to a month with selected firms. The same companies also receive other short-term specialists.

JETRO promotes buying missions to Indonesia. For 1991, JETRO projected that more than 400 Japanese business representatives would attend buying seminars in Indonesia to discuss product availability and Japanese standards. The representatives, who share costs with JETRO, are contacted through JETRO's network of prefecture-level "local internationalization centers" in Japan. In turn, JETRO partially finances eight to nine Indonesian missions to Japan a year to exhibit products. Prior to the actual Mission, JETRO brings a merchandizing expert to Indonesia to ascertain that the proposed products are appropriate for Japan markets.

Facilitation of joint ventures is a critical activity for JETRO. The director of JETRO was proud of achieving 17 joint ventures aligning Indonesian production with the Japanese market. The joint venture evolves through matching lists maintained in the Tokyo office with information supplied by the Djakarta staff. The local list often includes Indonesian companies that have received technical assistance from JICA or the IETC. In short, the way is paved for the eventual joint venture through early identification, hands-on improvements in production technology, and a preorientation of production elements toward the Japanese market. The linkage stresses product development, cost containment, quality control, and market connections. Throughout, the emphasis is on creating dependency on the Japanese market or markets beyond but through Japanese channels.

Although the Japanese efforts in Indonesia are the most extensive, other countries, notably the Asian Tigers, the Netherlands, and Germany have also demonstrated a certain degree of accommodation between aid and trade policies. Each country pursues commercial objectives by blending public and private activities within a coherent strategy. This coherence comes in part from the acceptance of the view that promotion of investment in Indonesia and (at least for Japan and the European countries) increased Indonesian exports to the home country promote the donor country's interests. Such strategies seem less concerned with Indonesian development objectives, though they do benefit from Indonesian success in policy reform.

4.2.2 Government Trade Promotion: Roles for Official Assistance

The study surveys indicated that exporters benefited in a limited way from services of government agencies, particularly the Ministry of Trade. Specifically, respondents indicated that they sought assistance early in their market entry through activities such as trade-selling missions, trade fairs for foreign buyers, and buyer searches. In the wake of an impressive series of trade-sector reforms, Indonesia is now grappling with the task of improving the effectiveness of institutions responsible for implementing new regulations and for providing relevant services supportive of the business community. A brief summary of the changing role of the Ministry of Trade illustrates this process.

The Ministry of Trade in Indonesia is attempting to move from a largely regulatory role to one that stresses promotion and facilitation of trade. With donor help, an effort is underway to raise the professional standards of Ministry personnel and to rethink the effectiveness of the Ministry's operational programs. A.I.D.'s Young Professional Program, for example, is a Ministrywide effort to provide on-the-job training to mid-level staff through lectures and workshops. Technical assistance is also provided in such areas as research skills, data analysis, information management, and documentation. Beyond this program, A.I.D. is considering future support for the reorganization of the Ministry of Trade, for specific policy studies, and for technical seminars, reflecting a current USAID/Indonesia emphasis on strengthening institutions charged with implementing export-enhancement policies.

In addition to policy formulation and research, the Ministry of Trade oversees the work of 34 trade representatives abroad, 27 provincial trade offices, and the trade promotion agency, NAFED. NAFED was established in 1971 to facilitate buyer contacts and, together with donors, to provide technical assistance to exporters in such areas as market information, trade regulations, and buyer searches. NAFED has staff in 18 countries where it has 24 commercial attach,s and 11 trade promotion centers. This network has not been particularly effective, however, and attempts to improve it have not been successful. Poor communication, unqualified personnel, an inadequate budget, and lack of a cohesive strategy have been identified as the major problems of NAFED.

Survey respondents cited two NAFED functions as the most helpful: Organization of trade Missions abroad and facilitation of foreign-buyer Missions to Indonesia. Of lesser note was support for the Buyer Reception Desk (BRD) and the Economic Support Board

(ESB). Despite the apparent lack of budget resources, NAFED supports and coordinates selling missions abroad (5 per year with up to 10 sellers per Mission). The Japanese, Germans, and the Dutch subsidize these activities, and the Netherlands has established a permanent Indonesian exhibit area. Germany and the Netherlands are in competition as the European gateway for Indonesian exports. Selling missions to the United States, in contrast, are rare and support is only infrequently available. Little information on buyer missions to Indonesia is available. There is little follow-up to these missions.

The BRD is another NAFED resource for exporters. Established in 1989, this 10-person office provides logistical and technical support to visiting buyer groups and individuals. A cursory look at activities of a group of 36 buyers visiting in July 1990, for example, indicated that 75 percent concluded a transaction in conjunction with their talks with the BRD. In some sectors (e.g., rattan) on-line buyer lists exist as well as buyer guides to selected industries, updated periodically. There is also a directory of Indonesian exporters, which is not comprehensive. The BRD does not have an effective budget. Fees generated by providing support are inadequate to expand this service or to maintain up-to-date data.

The Ministry of Trade has obtained considerable donor support, though with little interdonor coordination. The United Nations Development Programme (UNDP), for example, has had at least five projects with the Ministry of Trade, including professional training, trade policy technical assistance, trade mission support, trade statistics and documentation, planning, and quality control for agricultural commodities. The UNDP is still formulating an appropriate strategy. The World Bank has been working with the Ministry since the mid-1980s. The Bank's Export Development Project made available $13.5 million for export promotion technical assistance to go with $51 million in export credit. Activities included training of export promotion trainers, workshops, quality control education in testing centers, and several studies (e.g., export insurance, trading companies).

After a 1986 survey suggested a demand, the Ministry of Trade established the ESB, which was intended to provide subsidized services to improve production management and enhance marketing skills. Eligible firms apply to the ESB for cost-sharing assistance, which is generally well conceived. Such assistance has included market and feasibility analyses, training to improve marketing operations and production management, preparation of promotional materials, and support for promotional trips abroad. According to ESB, adapting products for the international market seems to be the key activity most needed by clients. Firms bear at least 25 percent, usually 50 percent, of the cost. Four of the six board members are from the private sector. In a self-evaluation in 1990, the ESB concluded that its program produced $24 in economic impact for every $1 of assistance. By 1991, approximately 190 companies benefited from this program. Currently, the World Bank is reviewing the prospect for a modest extension of support. The chief problem is that the ESB has not become self-financing and, without a mechanism for achieving sustainability, continued World Bank support is unlikely. The Bank, like the UNDP, Asian Development Bank, and A.I.D., is reviewing its next steps in export promotion. It seems likely that the Bank will renew its efforts at the policy and regulatory reform level rather than direct support to institutions such as the ESB.

5. FINDINGS

This study of export promotion services in Indonesia suggests that the country's efforts to restructure its economy and to liberalize trade and investment were essential to export growth. Once public goals and objectives were recast to achieve economic growth, the private sector responded quickly, both through an inflow of foreign capital and through restructured and more competitive Indonesian firms. Thus, the findings on A.I.D.'s assistance in the area of export promotion in Indonesia necessarily include both the policy domain and the various stages of facilitating transactions.

> Indonesia's phased trade and investment liberalization and deregulation was an essential precursor to transfers of technology, management expertise, commercial contacts, and finance, all of which spurred the development of an indigenous export capability. A.I.D.'s assistance to support deregulation formed the core of a fairly consistent, successful approach at the policy level to which was added a series of exploratory project activities related to firm-level export services.
>
> The market for fee-based export promotion services is multiproduct, institutionally differentiated, and competitive. At least as the sector had developed by 1991, there is no evidence of market failure in the provision of such services requiring public action.
>
> Government-subsidized efforts have some impact at the early stages of market entry and at the level of general information and buyer search facilitation, but the great bulk of such support comes from other sources. For more specific and more technical services, government initiatives have little value in comparison to private-sector sources.
>
> The bulk of production for export relies more heavily on internal resources and seller-buyer relationships than on externally hired export support services. The indigenous network of kin and associates provides important counsel and resources to exporters under "extra market" conditions. Fee-based business advisory services are still alien to many Indonesian exporters and are developing mainly in response to the demands of foreign investors.
>
> Most export growth in Indonesia is occurring through buyer-seller partnerships, or joint ventures, in which the buyer dominates the supply of production technology, management practices, training, and finance. Many of Indonesia's exports are thus heavily dependent on the buyer's marketing and technical capabilities. Such foreign

partners will retain interest as long as local costs of production remain low and products remain competitive. The long-term interests of such buyers are conditioned by the need for a quick exit in the event of shifts in the relative costs of production. It remains to be seen to what extent Indonesian firms are acquiring the capability to reduce this dependence and to move to higher value products as labor costs rise.

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